BEFORE THE

STATE OF CONNECTICUT

JOINT FINANCE COMMITTEE

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Testimony of Daniel Allegretti

For

Exelon Corporation

On

Governor's Bill No. 843 (LCO 3048)

Members of the committee, thank you for the opportunity to present this testimony today. My name is Daniel Allegretti and I am a Vice President for State Government Affairs with Exelon Corporation ("Exelon"). My testimony today is limited to section 19 of the bill which proposes to raise revenue for the State through an auction process that will arrange for the provision of retail electric service to customers that currently take Standard Service from their electric distribution company. Exelon supports section 19 with several manageable but essential modifications described below, and looks forward to working with the Committee to develop changes to the bill to make this process a success.

Exelon

By way of introduction, Exelon is a Fortune One Hundred company, headquartered in Chicago, Illinois, with operations and business activities in 47 states, the District of Columbia and Canada. Exelon owns Commonwealth Edison Company, the Baltimore Gas and Electric Company and PECO Energy Company, which combined own electric transmission and distribution systems that deliver electricity to approximately 6.6 million customers. Here in Connecticut we are best known through our retail brand, Constellation New Energy, which provides electricity directly to thousands of Connecticut businesses and residents and to over a million customers nationwide. Exelon is also the largest competitive power generator in the U.S., with approximately 35,000 megawatts of owned capacity comprising one of the nation's cleanest and lowest-cost power generation fleets, that includes over 3000 megawatts here in New England region. Exelon is a regular participant in the wholsale power solicitations conducted here in Connecticut and is a regular provider of Standard Service supply to CL&P and UI.

The Section 19 Standard Service Auction

Section 19 directs the procurement manager of the Public Utilities Regulatory Authority by July 2013 to issue a request for proposals for electric suppliers to provide a full service contract to blocks of residential and small commercial customers currently taking Standard Service supply from their distribution utility. These contracts will be for a term of three years with prices fixed for the first 12 months at a discount of at least 5% off the April 2013 Standard Service price. The customers will remain free to switch to a different supplier at any time.

Section 19 will no doubt be the subject of considerable debate before this Committee. Let me say at the outset that Section 19 is neither a radical approach nor a threat to the protection of consumers. Properly understood and properly structured it is no more than a simple and effective way of completing the ongoing transition from regulated monopoly electric service to a fully functioning competitive marketplace. What sets this proposal apart from what many other states have done is the inclusion of a creative twist that allows the state to earn a brokerage fee, that will help to address its budget needs, by accelerating in an organized manner a transition that is already taking place more slowly. Today, roughly half the customers in Connecticut have already elected to take their electric supply from a company other than their utility with nearly three quarters of the electricity in Connecticut being sold and consumed outside the Standard

Service. Moving the remaining Standard Service customers into the marketplace will invite more suppliers and more product offerings, enhance competition and create a stronger and more durable competitive retail market. It will also assist the State in meeting its current fiscal needs. For the proposal to succeed, however, we believe a few manageble but essential modifications are in order.

Accommodation of Existing Supply Contracts

Standard Service customers receive electricity from CL&P or UI which the utilities purchase in the wholesale market, mainly through contracts that adjust the quantity supplied to meet the actual Standard Service needs. Many of these contracts expire at the end of 2013 and the rest of them expire sometime in 2014. While retail customers are free to leave Standard Service at any time and purchase their electricity from another supplier, these wholesale supply contracts were entered into by both parties without provision for what amounts to the effective end of Standard Service altogether under section 19. Unless provision is made, the wholesale contract sellers can be expected to seek remedies for the effect of Section 19 on their agreements. Disputes, however, can be averted. The simplest mechanism is to delay the enrollment of customers under Section 19 until the expiration of the wholesale contracts in 2014. Alternatively, it may also be possible to negotiate buyout agreements for the cancellation of the contracts on terms that are fair and reasonable to both parties. The details of how to accommodate the existing wholesale supply contracts are best left to the Department; however, Section 19 should be amended to give the Department the clear authority and direction to make the necessary accommodations.

Auction Fees

One of the more unusual provisions of Section 19 is the proposal for the State to collect an auction fee from the winning bidders for each customer included in the customer block awarded. The payment of a brokerage commission or aggregation fee is a common commercial practice in the retail electric market and many of the private aggregators registered with the PURA collect a fee from suppliers for the service of bringing them together with a contracting customer. When these aggregators conduct an auction or solicitation on behalf of customers, however, it is the usual practice to fix and disclose at the outset the fee or commission that will be collected.

Section 19 is similar to such an arrangement with the State playing the role of broker or aggregator and collecting the auction fee. As proposed, however the bidders are asked to compete for blocks of customers by bidding both a price at which customers will be served and by bidding an auction fee. This presents two unecessary challenges. The first challenge is that it leaves the bidders and the procurement manager without a clear metric on which to award the winning bids. Will blocks of customers be awarded based on the highest auction fee or to the supplier offering the best retail price for electricity? The second challenge is that it leaves the State with substantial uncertainty as to how much revenue the auction will raise. Governor Malloy has indicated a desire to raise $80 million through the auction, however, as proposed the actual revenue to the State will depend on the bids form suppliers which will not be known until the auction is concluded. To address both these concerns Exelon recommends Section 19 be amended to adopt the more common commercial practice of fixing the auction fee in the

RFP and awarding the retail contracts based on the price to the customer. This will provide a single metric for making the auction awards and will enable the State to move forward with relative certainty as to the revenue the auction will produce. It has been suggested that a fee of $100 per customer is in line with the value to suppliers of acquiring a customer and will enable the State to realize approximately $80 million. These appear to be reasonable assumptions.

Price Cap

Under Section 19 bidders are required to fix prices for the first 12 months of a 3-year contract at a price that is not less than five percent below the Standard Service rate for such customer class as of April 1, 2013. Setting a price cap with an embedded discount for the first 12 months has the appeal of encouraging customer acceptance of an assignment to a new supplier. Unfortunately, a price cap also carries with it a very serious risk that the auction will fail. If wholesale power prices are lower at the time of the acution than they were when Standard Service supply was arranged then bidders will be able to participate in the auction. If, however, wholesale prices have moved higher at the time of the auction then bidders will be unable to participate.

What is important to bear in mind here is that the cost of electricity to customers in Connecticut, whether they are on Standard Service or whether they are on service from a retail supplier, will be priced based on prevailing conditions in the wholesale power market. If an auction fails because wholesale power costs have moved higher, then customers will remain on Standard Service. The current wholesale Standard Service supply contracts, however, will begin to expire at year's end and will be replaced with new contracts at prevailing wholesale market costs. In other words, Standard Service rates will not remain where they are in April 2013 either but will also move higher or lower over time with conditions in the market.

What this means is that transitioning from a wholesale Standard Service auction to a retail auction will not produce electric prices for customers that are either higher or lower. Moving to a retail auction will, however, produce two compelling benefits. First, it will raise a substantial amount of revenue for the State through the collection of auction fees from suppliers. Second, it will make for a more vibrant and durable retail marketplace in Connecticut. For customers who are already shopping there will be more suppliers making offers, more products to choose from and more overall competition. Customers leaving Standard Service will continue to receive competitively priced electricity and will have the advantages of an enhanced retail market available to them as well. For these reasons Exelon recommends that Section 19 be amended to remove the price cap on the first 12 months of service and instead award blocks based on the lowest fixed prices offered for 1the 2 months.

Customer Switching

As explained above, Section 19 puts the State in the role of an aggregator and enables the State to capture a brokerage fee for bringing together the supplier and the customer. Participation in the auction is attractive to suppliers because the costs of marketing and sales that would otherwise be expended to enroll a customer outside the auction are avoided through an auction award. Against this, however, is the fee the supplier must pay the State in connection with the auction. So long as the fee is commensurate with the value to the supplier of an auction award, the process will raise revenue for the State without imposing additional costs on the customer. The State is not imposing a tax but rather selling a valuable service to suppliers. Thus, the value of that service is key to the program's success.

One respect in which the Section 19 process differs from private aggregation transactions is the proposed retention by the customer of the right to switch at any time to another supplier. Normally, when an aggregator solicits fixed price offers from suppliers the customers are enrolled with the best offer for the full term of the fixed price. Customers who leave during the middle of the contract term are normally charged a termination fee, which for residential customers in Connecticut is capped by statute at $100. Without this termination fee the supplier is at risk for lining up supply for a customer only to find that the customer has left and the power must be re-sold, usually at a loss. Thus, sales entered into outside the auction process which include a termination fee will be more valuable to suppliers than sales made through the auction process with no termination fee.

The absence of the ability to assess a termination fee may have a chilling effect on auction participation. The value the aggregator brings to the supplier is the customer's commitment to purchase electricity at the offered price from that supplier for the offered term. With no commitment from the customer there is far less value to the supplier and there will be far fewer, if any, suppliers willing to participate in the auction and pay the auction fees. Exelon, therefore, recommends that Section 19 be amended to allow for the assessment of a $100 termination fee to customers who leave during the 12-month fixed price term. This is consistent with commercial practice, complies with the current cap on termination fees and will assure a successful auction outcome.

Conclusion

The transition from regulated monopolies to an open competitive marketplace in which customers shop for their electricity has come a very long way in Connecticut. It has taken longer than many of us thought it would and the transition is not fully complete yet. Before you are an opportunity to complete that transition soon and an opportunity to raise a considerable amount of revenue for the State in the process without collecting that revenue from customers or jeopardizing their supply of reliable and competitively-priced electricity. I hope you will embrace this opportunity and I hope you will allow us to work with you and with the administration to make the necessary modifications, fill in the details and ensure that this process works for all stakeholders.

Thank you.